

Office of Chief Counsel
Internal Revenue Service

memorandum

CC:SER:DEM:WAS:TL-N-3350-99
KEChandler

date: AUG 26 1999

to: Tom Petersen, Case Manager, Group 1106

from: Associate District Counsel, Delaware-Maryland District,
Washington, D.C.

subject: [REDACTED] - Interest Computation Issue

This is in response to your request for advice regarding the proper starting date for computing interest on an audit deficiency made to [REDACTED]'s [REDACTED] taxable year corporate tax Return. Prior to your written request, you discussed this issue with Richard Fultz of the Procedural Branch of the office of Assistant Chief Counsel (Field Service) and we have coordinated our response with him.

DISCLOSURE STATEMENT

This advice constitutes return information subject to I.R.C. § 6103. This advice contains confidential information subject to attorney-client and deliberative process privileges and if prepared in contemplation of litigation, subject to the attorney work product privilege. Accordingly, the Examination or Appeals recipient of this document may provide it only to those persons whose official tax administration duties with respect to this case require such disclosure. In no event may this document be provided to Examination, Appeals, or other persons beyond those specifically indicated in this statement. This advice may not be disclosed to taxpayers or their representatives.

This advice is not binding on Examination or Appeals and is not a final case determination. Such advice is advisory and does not resolve Service position on an issue or provide the basis for closing a case. The determination of the Service in the case is to be made through the exercise of the independent judgment of the office with jurisdiction over the case.

ISSUE

What is the proper starting date for computing interest on an audit deficiency made to [REDACTED]'s [REDACTED] taxable year corporate tax return?

FACTS

[REDACTED] (hereinafter "the taxpayer") initially reported an overpayment of \$ [REDACTED] on its income tax return for the tax year ended December 31, [REDACTED]. The [REDACTED] tax return was timely filed, under extension, on [REDACTED]. The taxpayer elected to have the [REDACTED] overpayment reported on its return credited to pay its estimated taxes for the following tax year, [REDACTED], but did not designate which installment of estimated taxes the overpayment was to pay. During the examination of its [REDACTED] return, the taxpayer agreed to an additional liability and assessment of tax in the amount of \$ [REDACTED] for the [REDACTED] taxable year.

The following information was reported by the taxpayer on Form 2220 for the [REDACTED] tax year:

<u>Installment</u>	<u>Cumulative Amount of Estimated Payments Required</u>	<u>Cumulative Amount Paid (Excluding [REDACTED] Overpayment)</u>
[REDACTED]	\$ [REDACTED] \$ [REDACTED]	\$ [REDACTED] \$ [REDACTED]

Counsel renders no opinion on whether the methodology chosen by the taxpayer to determine its estimated tax payments, or tax liability, for [REDACTED] is appropriate. The payments of estimated taxes for [REDACTED] of \$ [REDACTED] and \$ [REDACTED] reflected above were from funds other than the [REDACTED] overpayment.

For its tax year ended December 31, [REDACTED], the taxpayer initially reported an overpayment of \$ [REDACTED]. This amount included the [REDACTED] reported overpayment of \$ [REDACTED] and a reported overpayment of its estimated taxes for [REDACTED] which exceeded its reported tax liability for [REDACTED] by \$ [REDACTED] (\$ [REDACTED] + \$ [REDACTED] = \$ [REDACTED]). The taxpayer filed a claim for refund of the total reported overpayment of \$ [REDACTED], which was paid on [REDACTED]. The taxpayer claims that the refund was actually paid on [REDACTED].

DISCUSSION

The Service is entitled to interest on a deficiency in tax for the period that the tax was due and unpaid. I.R.C. § 6601(a); Avon Products Inc. v. United States, 558 F.2d 342 (2d Cir. 1978). If a deficiency in tax is determined after the taxpayer elected to credit a return overpayment against its estimated tax liability for the next succeeding year, interest will begin to accrue on the amount of the deficiency equal to the amount of the return overpayment as of the effective date of the credit election. H.R. Rep. No. 98-432 (Part 1), 98th Cong., 1st Sess. 190 (Oct. 21, 1983); see also, Rev. Rul. 88-98, 1988-2 C.B. 356. Section 413 of the Tax Reform Act of 1984 provides that overpayments of tax will be credited against the estimated income tax for the next succeeding year with full regard to Revenue Ruling 77-475, 1977-2 C.B. 476. Pub. L. No. 98-369, 98 Stat. 494. Revenue Ruling 77-475 provides:

[if] an overpayment of income tax for a taxable year occurs on or before the due date of the first installment of estimated tax for the succeeding taxable year, the overpayment is available for credit against any installment of estimated tax for such succeeding taxable year and will be credited in accordance with the taxpayer's election.

1977-2 C.B. at 476 (emphasis added). Accordingly, interest on the deficiency begins to accrue on the due date of the installment of estimated tax for the succeeding taxable year against which the overpayment was credited in accordance with the taxpayer's designation. H.R. Rep. No. 98-432 (Part 1), 98th Cong., 1st Sess. 190 (Oct. 21, 1983); see also Rev. Rul. 88-98, 1988-2 C.B. 356.

In light of May Department Stores Co. v. United States, 36 Fed. Cl. 680 (1996), the Service reconsidered the manner in which interest on a subsequently determined deficiency is computed under I.R.C. § 6601(a) when the taxpayer makes an election to apply an overpayment to the succeeding year's estimated taxes. When a taxpayer elects to apply an overpayment to the succeeding year's estimated taxes, the overpayment is applied to unpaid installments of estimated tax due on or after the date(s) the overpayment arose, in the order in which they are required to be paid to avoid an addition to tax for failure to pay estimated tax under I.R.C. § 6655 with respect to such year.

The date the overpayment becomes a payment on account of the succeeding year's estimated tax determines the date the prior year's tax became unpaid for purposes of I.R.C. § 6601(a). Prior to that date, the government has had the use of the funds with respect to the prior year's tax, and no interest is payable on the overpayment that is the subject of the taxpayer's election. See I.R.C. § 6402(b); Treas. Reg. § 301.6402-3(a)(5) and § 301.6611-1(h)(2)(vii). Interest should be charged from the point the prior year's tax is both due and unpaid. May Department Stores Co. v. United States, 36 Fed. Cl. 680 (1996), acq. AOD CC-1997-008 (Aug. 4, 1997); Avon Products, Inc. v. United States, 588 F.2d 342 (2d Cir. 2978); Rev. Rul. 88-98, 1988-2 C.B. 356.

Where the overpayment is not needed to satisfy any installment of estimated tax in the succeeding year, the overpayment would be treated as a payment of the succeeding year's income tax. Section 6513(d) provides that if any overpayment of income tax is, in accordance with I.R.C. § 6402(b), claimed as a credit against estimated tax for the succeeding tax year, such amount shall be considered as a payment of income tax for the succeeding taxable year (whether or not claimed as a credit in the return of estimated tax for such succeeding taxable year) and no claim for credit or refund of such overpayment shall be allowed for the taxable year in which the overpayment arises. See also I.R.C. § 6513(a) which provides that a payment of income tax made before the date prescribed for payment of the tax is considered paid on that date. The date prescribed for payment of tax is the time fixed for filing the return (determined without regard to any extension of time for filing the return). I.R.C. § 6151. Further, it is on this date that the overpayment is treated as a payment for purposes of computing interest on any overpayment of income taxes with respect to the succeeding year under I.R.C. § 6611(a) and (d). Thus, we conclude that the statute requires that an overpayment which the taxpayer elects to credit against estimated tax for the succeeding year must be treated as a payment against the next year's tax liability with an effective date no later than the due date of the next year's return.

No part of the [REDACTED] return overpayment was needed to avoid the addition to tax for failure to pay estimated income taxes under I.R.C. § 6655 for [REDACTED]. Therefore, interest on the subsequently determined deficiency for [REDACTED] begins to run from the date on which the return overpayment is applied to the [REDACTED] tax liability which is the unextended due date of [REDACTED] income tax return - [REDACTED]. It is on this date that the [REDACTED] deficiency became both due and unpaid.

CONCLUSIONS

As discussed above, it is the Service's position that even if none of the overpayment for the [REDACTED] is used to pay the estimated taxes for [REDACTED], interest on the subsequently determined deficiency for [REDACTED] begins to accrue no later than the due date for the [REDACTED] return, without regard to any extensions. The income tax return for [REDACTED] was due, without regard to extensions to file the return, on [REDACTED]. Consequently, interest on the [REDACTED] deficiency began to accrue on [REDACTED].

This advisory is being post reviewed by the National Office. We will advise you if they have any comments. If you have any question regarding this memorandum or want to discuss this issue further, please contact Karen E. Chandler directly at (202) 634-5403, ext. 224.

By: Bernard O. Brinsky for Bettie N. Ricca
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